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No. 85-558

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

ROBERT E. O'CONNOR AND GLADYS E. O'CONNOR,
Petitioners,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Federal Circuit

BRIEF FOR PETITIONERS

ALLAN I. MENDELSOHN
Counsel of Record
MARVIN L. SZYMKOWICZ
WARD & MENDELSOHN, P.C.
1100 17th Street, N.W.
Suite 900
Washington, D.C. 20036
(202) 785-0200
Counsel for Petitioners

Of Counsel
DWIGHT A. MCKABNEY
Apartado 3116
Balboa-Ancon
Republic of Panama
011-507-63-5316

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

58 pp

QUESTIONS PRESENTED

1. Whether United States citizen employees of the Panama Canal Commission (PCC) are exempt from taxation by the United States on their PCC salaries under Article XV(2) of the Agreement in Implementation of the 1977 Panama Canal Treaty which, by its terms, exempts such employees

> "from any taxes, fees, or other charges on income received as a result of their work for the Commission."

2. Whether diplomatic correspondence may be introduced by the Government immediately before oral argument in the court of appeals where the Government is itself the litigant and where it repeatedly refused the trial court's urgings to obtain and introduce such matters below.

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BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Federal Circuit is reported at 761 F.2d 688 (Pet. App. 1a-8a).[1] That opinion, which reversed the decision of the

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[1] References to material in the Petitioners' Appendix will be in the form: "Pet. App. ___". By Order entered February 24, 1986, this Court granted a Motion by Petitioners to dispense with the printing of a joint appendix. References in this Brief to the record below will be to the two volume Joint Appendix prepared for use in the United States Court of Appeals for the Federal Circuit, 10 copies of which

United States Claims Court, reported at 6 Cl.Ct. 115 (1984) (Pet. App. 9a-69a), is in direct conflict with the opinion of the United States Court of Appeals for the Eleventh Circuit in *Harris* v. *United States*, reported at 768 F.2d 1240 (1985) (Pet. App. 72a-86a), petition for certiorari pending.

JURISDICTION

The judgment of the Court of Appeals was entered May 10, 1985. A petition for rehearing was denied on July 3, 1985 (Pet. App. 70a-71a). The petition for a writ of certiorari, filed September 30, 1985, was granted by this Court on January 13, 1986. The jurisdiction of the Court is invoked under 28 U.S.C. §1254(1).

TREATY, EXECUTIVE AGREEMENT, AND STATUTE INVOLVED

Panama Canal Treaty between the United States of America and the Republic of Panama, September 7, 1977, T.I.A.S. No. 10030:

Article III

Canal Operation and Management

* * * * *

9. The use of the areas, waters and installations with respect to which the United States of America is granted rights pursuant to this Article, and the rights and legal status of the United States Govern-

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have been lodged with this Court by the Respondent. Reference to that appendix will be in the form: "App. ___". References to material in the Appendix to the U.S. Government's Brief, filed on December 3, 1985, acquiescing in the Petitions for Certiorari will be in the form: "U.S. App. ___".

ment agencies and employees operating in the Republic of Panama pursuant to this Article, shall be governed by the Agreement in Implementation of this Article signed this date.

Agreement in Implementation of Article III of the Panama Canal Treaty, September 7, 1977, T.I.A.S. No. 10031:

Article XV

Taxation

* * * * *

2. United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.

United States Code, Title 26, Section 894(a):

Income exempt under treaty.—Income of any kind, to the extent required by any treaty obligation of the United States, shall not be included in gross income and shall be exempt from taxation under this subtitle.

STATEMENT OF THE CASE

A. The Issue In Dispute: Historical Background Of The 1977 Treaty

On September 7, 1977, the United States and the Republic of Panama signed the Panama Canal Treaty of 1977. Article III of that Treaty provided that the "rights and legal status of United States Government agencies and employees operating in the Republic of Panama" shall be governed by a separate executive agreement titled "Agree-

ment in Implementation of Article III of the Panama Canal Treaty of 1977" (hereafter "the Implementation Agreement"). The Implementation Agreement was signed on the same day as the Treaty.[2] The basic issue before the Court involves the interpretation of one provision of that Agreement—Article XV(2), which states that U.S. citizens employed by the Panama Canal Commission (hereafter "the Commission") "shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission".

The 1977 Treaty supplanted the earlier Canal treaties of 1903, 1936, and 1955.[3] The 1903 Treaty ceded to the United States in perpetuity exclusive sovereign rights over the area that was called the Canal Zone. During the subsequent 74 years, Panama's dissatisfaction with that grant of sovereignty was said to be the reason for its recurring and increasingly acrimonious protests against the U.S. presence there. Throughout those 74 years, Panama's aspirations for eventual recovery of sovereignty over the Canal Zone were the fundamental irritant in her relations with this country.

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[2] The Treaty appears at T.I.A.S. 10030. The Implementation Agreement appears at T.I.A.S. 10031. A separate Implementation Agreement, covering military personnel and implementing Article IV of the Treaty, appears at T.I.A.S. 10032. No issue is raised here as to any difference in status between the Treaty and the Implementation Agreements. When the Senate was considering both documents as part of the advice and consent process, then State Department Deputy Legal Advisor, Mark Feldman, testified before the Senate Foreign Relation Committee that the Agreements "are an integral part of the treaty" and that "by giving its advice and consent to the treaties", [the Senate] authorizes the entry and brings into force those Agreements". Senate Hearings on the Panama Canal Treaty Before the Committee on Foreign Relations, 95th Cong., Pt. V, 1st Sess. (1977) at 117-121 (hereafter cited as "Hearings").

[3] Isthmian Canal Convention, November 18, 1903, 33 Stat. 2234, T.S. No. 431; General Treaty of Friendship & Cooperation, March 2, 1936, 53 Stat. 1807, T.S. 945; Treaty of Mutual Understanding & Cooperation, January 25, 1955, T.I.A.S. 3297, 6 UST 2273.

After the final phase of their negotiation of the 1977 Treaty, U.S. Ambassadors Ellsworth Bunker and Sol Linowitz testified at hearings conducted by the Senate Foreign Relations Committee. On September 26, 1977, Ambassador Linowitz described the treaty history of the Panama Canal as follows:

> "[The 1903 Canal Treaty] granted the United States rights in perpetuity to construct a canal within a zone 10 miles wide over which the United States would exercise, as the treaty says, the rights, power, and authority it would have if it were the sovereign.
>
> "Secretary of State Hay, who signed the treaty, candidly wrote to a leading Senator that the treaty was, in his words, and I quote, 'very satisfactory, vastly advantageous to the United States and, we must confess, with what face we can muster, not so advantageous for Panama'. The treaty was ratified in 1904, and construction of the canal was begun immediately. It was completed in 1914, after a brilliant engineering and scientific performance by American engineers, doctors, scientists, and builders who were determined to conquer the unconquerable and make the canal a reality.
>
> * * *
>
> "Now, while the canal has been a source of deep understandable pride to the United States, it has been a troubling and festering presence in Panama. Under the treaty, the United States established jurisdiction over the Canal Zone courts. It has established the zone's schools, jails, and its police force. It has set up what the Panamanians have regarded as a colonial enclave splitting their country in two and using 550 square miles of their best land, and the Panamanians have made known their resentment at the United

> States having done so pursuant to a treaty which was not even signed by a Panamanian."[4]

In a constituent newsletter, Senator Hollings described the U.S. role as follows:

> "There is no question, the United States rooked Panama back in 1903. We actively supported the revolution against Colombia by its Isthmus section after Colombia refused to ratify the treaty we wanted. We sent ships and troops and this guaranteed the outcome. Then we signed the treaty hurriedly before the official delegation objecting from Panama could even arrive in Washington. Signing for Panama was—not a Panamanian—but a French citizen who had not been in Panama for 17 years, and who returned to France immediately after the ratification."[5]

Secretary of State Cyrus Vance, also testifying in support of the Treaty, was asked whether Senator Hollings' historical summary was "generally on all fours with the understanding that you gentlemen have of how we got into this situation". He replied that it indeed "was generally on all fours with our understanding as to how we got into it".[6] The 1977 Treaty was the culmination of negotiations that began in 1964. In that year, as then Senate Foreign Relations Committee Chairman Sparkman observed, "rioting broke out in Panama and diplomatic relations were broken". President Johnson dispatched his then special envoy, Cyrus Vance, to the Canal Zone. In the aftermath of those events, based upon Mr. Vance's recommendations, President Johnson began to negotiate a new agreement with Panama on the canal. Each President since President Johnson, as Secretary Vance added, "has

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[4] Hearings, Part I at 20-21.

[5] *Id.* at 51.

[6] *Id.*

believed that it was essential to negotiate a new treaty and to put our relationship with Panama on a new and sounder footing".[7] In testifying about the final result of these negotiations, Secretary Vance stated that the new Treaty removed "one of the most difficult and exacerbating issues . . . and that is the issue with respect to how the U.S.'s presence will be handled there and the question of the Canal Zone itself and the question of sovereignty.[8]

It is against the background of those reports by high officials in the United States Government that the disputed provision of this international agreement should be viewed.

B. The Treaty Negotiations On The Subject Of Taxation

1. Background

Between the years 1921 and 1951, the salaries received by U.S. citizen employees of the Panama Canal, the Canal Zone Government, and other Federal agencies in the Canal Zone were effectively exempt from taxation by the U.S. Government. See §251, Internal Revenue Code of 1939 (prior to enactment of §220 of Revenue Act of 1950). Section 251 conferred a total tax exemption with respect to Panama Canal salaries paid to the U.S. citizen taxpayers—unless the taxpayer had substantial non-Panama source income (pursuant to a formula defined in §251). It may safely be said that most, if not all, of the salaried employees of the federal government working for the Panama Canal regularly qualified for the exemption. Beginning in 1951, their Panama Canal income became subject to taxation under amended §251 (i.e., §931(h) of the 1954 Code).

Notwithstanding the comparatively modest contribution to the Federal fisc made by this small group of American

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[7] *Id.* at 54.

[8] *Id.* at 37.

taxpayers—numbering 1,895 in 1980 and 1,360 in 1985[9]—the question of the right to tax them was the subject of considerable dispute during the Treaty negotiations. It was also among the very last issues to be resolved. As of June 24, 1977, Secretary of State Vance advised that all other Treaty questions had been settled and that the matter of "economic arrangements" (which included the tax issue) was "the major remaining issue relating to the Canal negotiations" (App. 163).

2. The Panamanian Position in the Negotiations

Negotiations on the taxation issue were strained and, at times, contentious. Both the United States and Panama claimed the right to tax the U.S. citizen employees. Panama viewed that right as an essential attribute of its restored sovereignty over the Canal Zone. As a sovereign, it had the right to tax income earned in and from its territory. Consistent with that view, the Panamanian negotiating team proposed the direct imposition of Panamanian taxation on all Americans employed by the Panama Canal Commission. *See* Kozak affidavit (App. 89). On July 11, 1977, Minister Aristides Royo, a member of the Panamanian negotiating team, summarized Panama's position as follows (App. 120-21):

> "Also, in another paper that we submitted to you, we brought out the need for U.S. citizen employees who worked for the entity [i.e., the Panama Canal Commission], which will be operating the Canal after the treaty, to pay income tax to Panama, and the reason is very simple. These employees, despite the fact that they are United States nationals, are employees who are working outside the United States and in territory that will not be subject to the jurisdiction of the United States, and their salaries will be generated

[9] Annual Report, Panama Canal Commission, Fiscal Year 1980, p. 21; Govt. Brief Acquiescing in Certiorari Petitions, at 12

not from U.S. Treasury funds, but from the activities involved in operating the Canal; and accordingly, and furthermore, because these persons, as you know and as we have already agreed, have the right of free movement throughout the breadth of our country, and will receive all due attention from us in every respect whether it is hospitals, social matters, or travel in our country, these are people that ought to pay our country, as do the remainder of those citizens and persons working on our soil, that they should pay income tax. You said that you were going to study this problem, and we are again hoping for a positive response from you in order to arrive at the conclusion of a treaty between our two countries."[10]

While insisting on its own right to tax, Panama was not inflexible on the issue of whether the U.S. could also tax. Thus, during an earlier session, on June 30, 1977, Mr. Royo suggested a division of tax revenues (App. 117):

"So on the basis of that credit, the tax credit, on the basis of that difference that could be provided to determine the difference with the Panamanian taxes, which are lower—the United States would receive a part of the tax and we would be receiving the other part. And in that way we would get all of the amount we expect from the income tax—this might be a formula that might be found to be satisfactory.

"We will be willing to provide additional information later on, on this topic."

3. The U.S. Government's Position In the Negotiations

The U.S. negotiating position was stated by Ambassador Linowitz during the session of June 30, 1977. He in no

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[10] The State Department has never released that "another paper" referred to by Mr. Royo in his first sentence as having previously been "submitted" to the U.S. Government.

way took issue with Panama's claim of right to tax based upon territorial sovereignty. Rather, he indicated that the U.S. objected to the Panamanian proposal because depriving the U.S. of the right to tax would mean a loss of revenue for the U.S. Treasury. His statement was (App. 117):

> "Then it would be a cost to the United States. That is the point. What you are saying is: it would not be an additional charge on the employees, but would represent a loss to the United States of taxes that would otherwise be paid in the United States. That's what you are saying, aren't you?"

Ambassador Linowitz indicated that the U.S. would study the issue and let the Panamanians "know what further work we have done" (App. 116).

4. The U.S. Government's In-House Position

In contrast to what they told the Panamanians, the American negotiating team held a different view. They considered the potential loss of revenue not to be significant. By means of a U.S. Treasury Department memorandum entitled "Rebating to Panama U.S. Income Tax on Canal Zone Taxpayers" (App. 159), the U.S. representatives were informed that only a modest amount of tax revenue was involved. The memorandum, which was dated June 29, 1977 and prepared for the discussion of tax and revenue issues at the 21st round of the negotiations, reported that Americans residing in the Canal Zone paid little or no taxes and the total of lost revenue would be about $600,000.

In a State Department memorandum from Secretary Vance to the Panama Review Committee, it was estimated that, by taxing the U.S. employees, Panama would realize revenues of "not more than $3 million per year". *See* Memorandum, July 19, 1977 (App. 151-52). At a later point, the State Department estimated that Panama "would re-

alize only $2-3 million per year" from taxing these employees, but that this would "set a bad precedent" (App. 164). The Department was also concerned that this "would be the type of issue which treaty opponents could use to considerable advantage" (App. 162).

As noted in a Department briefing paper of July 8, 1977 (App. 130), the American team recognized that the tax dispute was a matter principally of sovereignty, not of revenue:

> Panama may be raising this as an issue to assert its 'sovereign right' to tax persons resident within its jurisdiction. The money involved is not important to the GOP [Government of Panama], but the principle is. At current Panamanian tax rates, tax payments by U.S. employees would total approximately $2 million per annum (average U.S. employee taxable income is $11,000 plus). . . . . [remainder of paragraph still classified] A concession to Panama on this issue could result in demands from other countries for similar treatment."

Consistent with this view, the U.S. team also rejected still another Panamanian suggestion, advanced about July 19, 1977, that Panama not tax U.S. employees until "three years after entry into force of the treaty" (App. 128, 151-152, 154).[11]

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[11] Two Confidential Memoranda prepared by then Secretary of State Vance sometime around July 19, 1977, put the issue in these terms (App. 151-152, 164):

> Panama has proposed that effective three years after entry into force of the treaty the United States citizens employed by the Canal Administration pay income taxes to Panama on their salaries and other income collected in Panama. It estimates these taxes at $7-10 million a year.
>
> While we have told Panama that it would be most difficult for the United States to acquiesce to Panamanian taxation of its U.S. citizen employees, we *could* do so if we chose. However, United

C. The Gaps In The Negotiation Record

The Department of State represented to the Claims Court that, after July 18, 1977, there is no contemporaneous record of any of the negotiations on the issue of taxing the U.S. citizen employees. *Coplin*, *supra* (Pet. App. 28a-29a, 34a). Accordingly, with minor exceptions (e.g., App. 161-62), there is no record of the position papers or discussions within the U.S. team, nor any information showing how the language of Article XV was proposed, discussed or adopted. Nevertheless, when the treaty negotiations ended in August 1977, the language of paragraph 2 of Article XV somehow had reconciled the sharply conflicting objectives of the two nations.

It is clear that, however the dispute was resolved, it was done in haste. As late as the session of July 11, the American negotiators still had not given the Panamanians a paper showing the U.S. position in writing (App. 126-27):

> MINISTER ROYO: Do you have anything on income tax?
>
> AMBASSADOR BUNKER: Yes.
>
> MR. WYROUGH [a U.S. negotiator]: Yes, we do.
>
> AMBASSADOR LINOWITZ: We don't have a paper. [. . . here a half page of the classified document was deleted . . .] Now, on the income-tax question we do not have a paper. . . . . we have no authority to accede to your request on this score.

Similarly, as of July 18, the U.S. had still not given Panama the text of a proposed Article XV but, instead,

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States Government employees are exempted from host country income taxes throughout the world. Making Panama an exception would set a bad precedent for U.S. Government operations in other foreign countries. Secondly, we estimate that revenue generated from such taxation would amount to not more than $3 million per year (emphasis in original).

was merely referring orally to a provision in the Status of Forces Agreement (i.e., Article XVI of what became the Agreement in Implementation of Article IV of the 1977 Treaty) (App. 156, 158, 178). Even as late as the date of the State Department's secret cable of August 3, 1977, the matter was still unresolved (App. 99, 166). Yet, within the next two to three weeks, the negotiations were concluded. On September 7, 1977, the Treaty was signed.

D. The Failure Of The Government To Seek Clarification Before Ratification Of The Treaty

By September 21, 1977, attorneys in the Treasury Department realized that Article XV(2) would create an exemption from United States, as well as Panamanian, taxes (App. 58-59). They recommended that the language be clarified. Their recommendation was not acted upon. Later, during hearings before the Senate Foreign Relations Committee, Senator Stone raised the same question—referring to what he described as the "glee" shown by Canal Zone residents who also had read Article XV(2) as exempting their salaries from taxation. The Senator questioned the State Department's Legal Advisor, Mr. Herbert Hansell, as to whether the language should be clarified if an exemption was not intended. Mr. Hansell replied that something would be done (Hearings, Part I at 268-269) (U.S. App. 10a-12a). The record is devoid of evidence that anything was ever done by the Government prior to February 1985.

E. The Differing Panamanian Explanations As To What Happened In August 1977

1. The Initial Panamanian Views

There is evidence showing the meaning given by certain Panamanian representatives to the phrase "exempt from any taxes". By correspondence dated December 13, 1983, Mr. Demetrio B. Lakas, a former President of Panama, and Mr. Juan Antonio Tack, a former Minister of Foreign

Relations of Panama, both stated their views that Article XV(2) was intended to create a [illegible]onal tax exemption (App. 188, 190).

Similarly, in an affidavit executed on March 2, 1984, one of Panama's principal treaty negotiators, Dr. Carlos Lopez-Guevara, stated that only during the last negotiation session sometime in August did the U.S. for the first time provide to Panama a written proposal for the text of Article XV (App. 192-93). Lopez-Guevara further stated that paragraph 2 of Article XV was viewed by Panama as compelling "both Panama and the United States of America not to tax United States citizens by reason of their work with the Panama Canal Commission".

2. The U.S. Government Declines to Obtain Views From the Panamanian Government

During February and March 1984, when this case was before the Claims Court and the views of Messrs. Lakas, Tack and Lopez-Guevara were already matters of public record, the Claims Court made a determined effort to ascertain whether the U.S. Government could or would obtain a view on the issue from the Panamanian Government. On February 23, 1984, after expressing some scepticism as to the persuasiveness of the U.S. Government's asserted position, the Claims Court continued the case for two weeks to give the Government an opportunity "to consider supplementing the record by obtaining an indication from Panama as to its intentions in agreeing to the language of Article XV" (Pet. App. 64a). Thereafter, and as described in the Court's opinion (*Id.*):

> "At the next hearing on the matter, [Government] counsel informed the court that no clarification would be requested or obtained from Panama (Mar. 8 Transcript at 3, 8). The court then took the unusual step of inviting an appearance by a more senior attorney to ensure that the implications of this decision were fully understood and appreciated by [the Government].

> [Government] counsel and her supervisor [Mr. Peyser] appeared at a hearing later the same day and the court once again stated that it found plaintiff's presentation persuasive but urged [the Government] to supplement the record by obtaining clarification from Panama or through some other means. *Id.* at 26-27, 39-40, 43-45, 49-50. Despite numerous statements by the court that it would decide the case in favor of plaintiff on the record as presented, [the Government] steadfastly refused the opportunity to supplement the record."

Government counsel specifically represented to the Court, during the March 8, 1984 hearing, that the United States did not think "the opinion of any official in Panama in 1984 is persuasive".[12]

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[12] A portion of the court's colloquy with Government counsel is reprinted below (Transcript, pp. 43-47, March 8, 1984):

> Court: I am giving you the opportunity to obtain from Panama their understanding as to the meaning of this provision. That is what I gave your attorney two weeks ago. It is done all the time for one Government to get a diplomatic note from another Government saying we had a Treaty provision and this is what it means. If you don't want to get it, I will draw whatever inferences can be drawn from the refusal to obtain that.
>
> Mr. Peyser: I think the case should be decided on the materials before the Court.
>
> Court: So I am going to ask you one more time, Mr. Peyser, do you wish to take advantage of the opportunity to supplement the record by obtaining a clarification of Panama's understanding of the Treaty language? If you wish, have a few days or a week to go back and check on that. I will give it to you, but I want a concise and clear yes or no answer from the United States.
>
> Mr. Peyser: No. No., your Honor.
>
> • • • • •
>
> Mr. Peyser: I don't [think] the opinion of any official in Panama

3. The U.S. Government Gives Panama An "Historic" $30 Million Direct Grant Of Aid and Obtains the Views of the Panamanian Government

On December 24, 1984, the U.S. Government gave Panama a direct grant in aid of $30 million. U.S. Ambassador to Panama, Everett Briggs, was reported as having described the grant as "historic" because it was the first time the U.S. had ever made such a direct grant to Panama. (Annex C to Motion by Appellees to Strike, filed March 4, 1985.)

On Thursday, February 28, 1985, one working day prior to oral argument in the Federal Circuit on Monday, March 4, 1985, the Government filed its reply brief. Without prior notice, the Government attached to its reply brief three nearly identical letters from former Panamanian officials who were members of the Panamanian negotiating team. These letters, which were accompanied by a transmittal note from then Panama Foreign Minister Fernando Cardoze, stated that the provision in issue was "drafted exclusively with respect to the tax exemption that the Republic of Panama would grant to U.S. citizen employees" and "resulted from negotiations which did not deal

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in 1984 is persuasive.

Court: . . . All I can gather is that you don't think you are going to get from Panama the interpretation that you want.

Mr. Peyser: I have no idea what the response would be from Panama.

Court: Well, would you like to go find out?

Mr. Peyser: I decline the invitation to do that. I understand you are asking if we would like to do that, and the answer is, no. I don't think it would be appropriate or necessary.

with the United States authority to tax the individuals mentioned therein" (U.S. App. 4a-9a).[13]

F. The United States View

The gist of the United States position in the courts below has been that, notwithstanding the continued sharp differences between the two nations on the issue of whether Panama enjoyed the sovereign right to tax, the Panamanians simply capitulated, withdrew their claim of a sovereign right to tax, and agreed that only the United States could assess such taxes. Regarding the views expressed by Messrs. Lakas, Tack and Lopez-Guevara, the United States argued below that this "simply is an opinion after the fact. It's not contemporaneous. It was prepared in preparation of this lawsuit" (Transcript, Feb. 13, 1984 at 26).[14]

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[13] On March 4, 1985, shortly preceding oral agrument, the taxpayers moved unsuccessfully to strike the correspondence from the record, arguing that they had had no opportunity to inquire into the provenance of the correspondence or its validity. At issue was the peculiar nature of the letters themselves plus the fact that the authors of two of the letters did not state that they participated at all in the Article XV(2) negotiations, and the author of the third letter claimed to have had a role only in the negotiation of Article XVI(2) of the Article IV Implementing Agreement. In addition (and as is more fully discussed below at pp. 40-42), former Panama Foreign Minister Fernando Cardoze had earlier expressed a contrary official view to the effect that U.S. citizens enjoyed a binational exemption under Article XV(2).

[14] In various district counts that ruled for the Government in similar cases brought prior to the litigation below, the Government introduced into evidence an affidavit of a Mr. Michael Kozak who is now a State Department Deputy Legal Advisor. In 1977, Mr. Kozak was a member of the U.S. team negotiating the Treaty, but "was not privy to the actual negotiations on the tax exemption issue". *Harris* v. *United States* (Pet. App. 82). Mr. Kozak's affidavit (App. 87-90) concluded that Article XV was intended to create an exemption only from the payment of Panamanian taxes. Although various of the district courts that had earlier ruled for the Government relied principally on Mr. Kozak's affidavit, the Government in the Claims Court below conceded that Mr.

G. The Principal, Relevant Provisions Of The 1977 Treaty

The Treaty was ratified by President Carter on June 15 and by Panama on June 16, 1978. It entered into force on October 1, 1979 and will terminate on December 31, 1999. Article III(1) recognizes Panama as the "territorial sovereign" and grants the United States the "rights to manage, operate, and maintain the Panama Canal, its complementary works, installations and equipment and to provide for the orderly transit of vessels . . .". Article III(3) provides for the creation of a Panama Canal Commission by means of which the two countries are to carry out their responsibilities under the Treaty.

Although the Commission is constituted under Federal law and is denominated as a U.S. Government agency, the Treaty requires that it be managed by a binational supervisory board. Five of the board members are Americans. The other four must be Panamanians who are nominated by the Government of Panama and cannot be removed without Panama's consent. The two executive officials of the Commission are an Administrator and a Deputy Administrator. Until 1990, only the Deputy need be Panamanian (nominated by his government). Thereafter, until the treaty expires, the Administrator must be a Panamanian and the Deputy an American. Article III(8) provides that there shall be a growing participation of Panamanian nationals at all other levels and areas of employment in the Commission. Finally, Article X(3) requires the United States, within the first five years after the Treaty enters into force, to reduce the number of U.S. citizen employees by 20%.

Kozak's affidavit "may not be used to divine the purpose of Article XV" (Pet. App. 35a, n. 16). The Government later disavowed Mr. Kozak's affidavit presumably because the Government could not consistently argue that Mr. Kozak's affidavit was probative while saying that Mr. Lopez-Guevara's affidavit was nothing more than "an opinion after the fact . . . prepared in preparation of this lawsuit".

The treaty and related agreements also contain substantial economic benefits and concessions for Panama. The United States agreed to pay from Canal operations four separate annuities, three of which would be fixed and one that would be based upon, and vary with, the amount of vessel traffic passing through the Canal. The value of these Canal annuities was estimated in 1978 at from $50 to $90 million per year for the duration of the Treaty. There were also undertakings by the United States to extend housing investment guarantees up to $75 million; loans, loan guarantees, and insurance up to $200 million through the Export-Import Bank; and $50 million in repayment guarantees under the foreign military sales program to facilitate the purchase by Panama of defense articles and services. Article XIII provides that upon termination of the Treaty, the Panama Canal shall be given to the Republic of Panama in operating condition and free of liens and debts. The estimated replacement value of property that has been or will be given to Panama is $8 billion. *See* S. Exec. Rep. No. 95-12, 95th Cong., 2nd Sess., 1978, at 91 et seq.; Exchange of Notes between Panama and the U.S., September 7, 1977.

H. Procedural Posture Of Litigation

Petitioner Robert O'Connor is a U.S. citizen employee of the Panama Canal Commission. The O'Connors paid their income taxes for the year 1980 and then sued for refund in the Claims Court based on the Article XV(2) exemption. On July 30, 1984, the Claims Court (Chief Judge Kozinski) entered summary judgment in the *Coplin* case (Pet. App. 9a) and separate judgments for the O'Connors and Mr. and Mrs. Jack Mattox, all of which cases are consolidated herein. In addition, the Claims Court suspended action on all pending Article XV(2) refund suits until the outcome of *Coplin*. There are now more than 200 taxpayer suits pending in the Claims Court, awaiting the outcome of this appeal.

The Government appealed the Claims Court action to the U.S. Court of Appeals for the Federal Circuit. By opinions entered on May 10, 1985, the Federal Circuit reversed the Claims Court. Writing for the five-member panel, Judge Bissell concluded that, in view of the "letters from the Panamanian team that negotiated the Implementation Agreement"(Pet. App. 7a):

> "[T]he record now reveals the intent of each government. Since both treaty parties agree that paragraph 2 was not intended to create an exemption from United States domestic taxation, the trial court's decision cannot be upheld."

The opinion held that the letters could properly be received into evidence because of the court's power to take judicial notice of "the public acts and proclamations of (foreign) governments" (Pet. App. 6a). In a concurring opinion of Judge Nies, in which Judges Rich and Baldwin joined, the court concluded that it was not necessary to consider the evidence provided by the diplomatic correspondence, inasmuch as the words "by the Republic of Panama" should simply be inserted into the title of Article XV—even though, as drafted, that title is simply "Taxation" (Pet App. 8a).

Mr. and Mrs. Ralph Harris, also U.S. citizen employees of the Commission, filed a similar refund suit in the U.S. District Court for the Southern District of Georgia, seeking a refund of $6,647.00 for taxes paid on 1979 income. On March 21, 1984, Judge Dudley H. Bowen entered judgment for the Harrises on the basis that Article XV(2) is "needful of no interpretation. It says what is says." 585 F.Supp. 862, 863. The Government appealed Judge Bowen's decision to the U.S. Court of Appeals for the Eleventh Circuit. As it did in the Claims Court, the Government submitted the three letters to the Eleventh Circuit. On August 14, 1985, a unanimous panel of the Eleventh Circuit affirmed Judge Bowen (Pet. App. 72a-86a). The Court considered

the Federal Circuit's decision in *Coplin* and declined to follow it. The Court rejected the Government's "suggestion that self-serving evidence outside the record [i.e., the three letters], for which additional explanation is required, can be considered by this Court". In any case, so the Court added, a full reading of the Treaty and the available legislative history compels the conclusion that " 'exempt from any taxes' meant just that" (Pet. App. 76a, 79a). The Government's petition for certiorari is presently pending disposition (No. 85-1011).

SUMMARY OF ARGUMENT

1. It was error for the Federal Circuit to accept and consider on the merits the diplomatic correspondence obtained by the United States on the eve of oral argument below. The Claims Court had earlier entreated counsel for the United States to secure a statement from the Government of Panama of its interpretation of Article XV(2). The United States refused, representing that it would not be "appropriate or necessary" to do so. Its contradictory position before the Federal Circuit created a judicial estoppel against introduction of the material.

The doctrine of judicial estoppel prohibits litigants from taking inconsistent positions before different Courts with respect to the same set of facts. It is meant to protect Courts and litigants from parties that would otherwise vary and contradict themselves where expediency dictates. In the instant case, the application of judicial estoppel also would have the salutary effect here of preventing the United States from using diplomacy to influence the outcome of domestic litigation.

The late introduction of the diplomatic correspondence should also have been barred by the prohibition on supplementing the trial record on appeal. By considering the new material and treating it as conclusive on the question of the intent of the Panamanian negotiating team, the

Federal Circuit deprived the O'Connors and their co-petitioners of an opportunity to develop a proper adversary trial record on the diplomatic correspondence.

2. Article XV(2) must be construed according to the rule that the plain meaning of a legal instrument is normally controlling. The language of Article XV(2), on its face, creates an exemption from "any taxes". By contrast, other provisions of the Treaty documents specifically define rights and obligations that are to apply to Panama alone. Similar agreements between the United States and foreign governments specifically define the circumstances under which only the host country is prohibited from imposing taxes. Article XV(2)'s radical departure from this established patttern of international agreements confirms that it was intended to be a binational exemption.

In July 1984, at a meeting of the PCC supervisory board, Panamanian members of the board expressed the official view that Article XV(2) exempted U.S. citizen employees from U.S. income taxation. Those members were then Foreign Minister of Panama Ortega and soon to become Foreign Minister Cardoze. Dr. Cardoze was the same individual who, a few months later, would sign the diplomatic correspondence submitted to the Federal Circuit. That court committed reversible error in refusing to consider the transcript of the board meeting tendered in the O'Connors' petition for rehearing.

This Court's case law on treaty interpretation supports a plain meaning reading of the term "any taxes" as creating a binational exemption. No case relied upon by the United States in the proceedings below sanctions a departure from the plain meaning of a provision where there is no ambiguity in the treaty or related documents.

The history of the Article XV(2) negotiations confirms the plain meaning interpretation. The final Article XV(2) language was presented for the first time in August 1977, shorn of its earlier references to taxation "as provided by

Panamanian law". It was accepted by both countries as a compromise formulation under which neither nation would tax. Such a result accommodated the objectives of both countries: the U.S. did not wish Panama to tax the income of American citizens whom the U.S. viewed as employees of a U.S. agency; and Panama did not wish to allow the U.S. to assert the sovereign right to tax individuals who were residing in Panama and employed by a binational enterprise.

ARGUMENT

I. The Appellate Level Introduction Of Diplomatic Correspondence Was Precluded By The Doctrine Of Judicial Estoppel And The Normal Prohibition On Supplementation Of The Trial Record On Appeal

A. The Government's Representations To The Claims Court That It Would Be Improper And Unnecessary To Seek A Diplomatic Note From Panama Judicially Estopped It From Presenting Such A Note To The Federal Circuit

As related in the O'Connors' statement of the case, the Claims Court repeatedly asked the United States to supplement the trial record with a statement from the Government of Panama. The United States "decline[d]" the Court's invitation, stating that, coming in 1984, such a statement would not be "persuasive" on the merits and that the process of soliciting it would not be "appropriate or necessary".

The United States specifically requested that the Claims Court decide the action based on the "materials before it" and agreed to the Claims Court approach of not relying on any of the post-negotiation statements of either of the contracting nations (Pet. App. 35a-36a, n. 16). As a result, the Claims Court analysis was based on the Treaty language and the negotiating transcripts.

The representations to the Claims Court by the United States created a judicial estoppel that should have barred

any appellate consideration by the Federal Circuit of the diplomatic correspondence. The Court's reliance on the correspondence was reversible error.

1. The doctrine of judicial estoppel prohibits a party from advancing inconsistent positions with respect to the same facts before different courts. *Himel* v. *Continental Ill. Natl. Bank*, 596 F.2d 205, 210-211 (7th Cir. 1979); *In re Yarn Processing Patent Validity Litigation*, 498 F.2d 271, 279 (5th Cir. 1974), *cert. denied* 419 U.S. 1057, 95 S.Ct. 640, 42 L.Ed.2d 654 (1974). The doctrine prevents litigants from "playing 'fast and loose' " (*Scarano* v. *Central R. R.*, 203 F.2d 510, 513 (3d Cir. 1953)), or "blow(ing) hot and cold" (*Ronson Corp.* v. *Aktiengesellschaft*, 375 F.Supp. 628, 630 (S.D.N.Y.1974)) with the courts. Its purpose is to "protect the integrity of the courts and the judicial process" from litigants who would seize upon any expedient to advance their case. *United Virginia Bank* v. *Saul Real Estate*, 641 F.2d 185, 190 (4th Cir. 1981), quoting from *Duplan Corp.* v. *Deering Milliken, Inc.*, 397 F.Supp. 1146, 1177-1179 (D.S.C. 1975). See also *Bower* v. *O'Hara*, 759 F.2d 1117 (3rd. Cir. 1985); *Donovan* v. *United States Postal Service*, 530 F.Supp. 894 (D.D.C. 1981).[15]

Although judicial estoppel is not yet a universal doctrine, it has been approved in dicta by this Court. See *Huffman* v. *Pursue, Ltd.*, 420 U.S. 592, 606 n. 18, 95 S.Ct. 1200, 1209 n.18, 43 L.Ed.2d 482 (1975). The doctrine has also been endorsed by most United States Courts of Appeal (see *supra*) and an increasing number of state courts. See, for example, *Associated Hospital Service* v. *Pustilnik*, 497 Pa. 221, 227, 439 A.2d 1149, 1151 (1981); *Mecham* v. *City*

[15] Cf. also *Hohri* v. *United States*, 782 F.2d 227 (D.C.Cir. 1986) (government concealment of information tolled statute of limitations), and *Belton* v. *Commissioner*, 562 F.Supp. 30 (D.D.C. 1982) (government misconduct in connection with tax lien levy that lulled third-party claimant not to timely file claim of entitlement as to levied funds estopped IRS from relying on otherwise applicable statute of limitations).

of Glendale, 15 Ariz.App. 402, 489 P.2d 65, 67 (1971); *Aetna Life Ins. Co.* v. *Wells*, 557 S.W.2d 144, 147 (Tex.Civ.App. 1977), writ of error refused, 566 S.W.2d 900, 901 (Tex. 1978) (per curiam).

2. While the United States has neither explained the genesis of the diplomatic correspondence nor conceded that U.S. officials were responsible for obtaining it, its appearance on the eve of the oral argument before the Federal Circuit cannot be coincidental. It strains credulity to believe that the Government of Panama, seven years after the Panama Canal Treaty was executed, was suddenly impelled, absent inducement by our State Department, unilaterally to express its views about a single provision of one Treaty Implementation Agreement. Also, while there is no evidence of a direct cause and effect relationship between the sudden appearance of the diplomatic correspondence and the "historic" $30 million foreign aid grant to Panama only some eight weeks earlier, the temporal proximity of the two events again hardly suggests a coincidence.

Such facts support the application of judicial estoppel against the United States. Application of this doctrine requires (1) an unqualified assertion of law or fact by a party in one judicial proceeding, and (2) an intentional contrary assertion by the same party in a subsequent judicial proceeding. *Bower* v. *O'Hara*, *supra*. Those elements are present here.

Before the Claims Court, the United States made the unqualified assertion that, as a matter of diplomatic practice it would not be "appropriate" to obtain a statement from the Government of Panama. The United States also maintained that it was not "necessary" to obtain such a statement. Indeed, the Government effectively conceded both before the Claims Court (Pet. App. 35a-36a) and before the Eleventh Circuit in *Harris* (Pet. App. 76a) that, as a matter of law, the Article XV(2) issues should be

decided without reference to *any* post-negotiation statements of any of the Panama Canal Treaty negotiators.

Before the Federal Circuit the United States took directly contrary positions—i.e. (a) that a statement from Panama was appropriately obtained, and (b) that the content of the statement, consisting of present day assertions of three individuals (two of whom were not even involved in the Article XV(2) negotiations), was proper matter to consider in interpreting Article XV(2). In other words, after telling the Claims Court that it was not "appropriate or necessary" to obtain any statement from Panama, it procured a statement from Panama for use before another Court.[16]

This is precisely the type of conduct that judicial estoppel is meant to prevent—the formulation of *ad hoc*, inconsistent litigation positions calculated to win at any cost and without regard to an accurate rendering of the facts and law. For that reason, the Federal Circuit should have judicially estopped the United States from introducing the diplomatic note.

3. Apart from its judicial dimension, the United States' conduct also taints the foreign policy process. The Government has used the tools of diplomacy not for any legitimate foreign policy purpose, but to bail itself out of a difficult, embarrassing and potentially costly domestic lawsuit.

4. A final consideration favoring the application of judicial estoppel was raised in the Claims Court opinion. In Federal tax refund suits prior to *Coplin*, *O'Connor*, and *Mattox*, the United States tendered an affidavit of Michael

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[16] Even in its opening brief below (at 46), the United States justified its refusal to ask Panama for its interpretation of Article XV(2) "because the Panamanian interpretation would be of little relevance even if it should prove to be contrary to the United States' position".

Kozak, now a deputy legal adviser at the State Department (Pet. App. 35a-36a, n. 16; App. 87-90). In 1977, Mr. Kozak was a member of the Department's Panama Canal Treaty negotiating team. The Kozak affidavit characterized the purpose of the negotiations surrounding Article XV(2) as limited to creating an exemption from Panamanian taxation. *Id.*

Below, the United States abandoned its reliance on the Kozak affidavit, admitting that Mr. Kozak was not present at the Article XV(2) negotiations. As the Claims Court noted:

> Defendant now concedes that the Kozak Affidavit may not be used to divine the purpose of Article XV. Feb. 23 Transcript at 30-32. Defendant has also suggested that reliance on the Kozak Affidavit to support its proposed finding as to intent was inadvertent. Reply Brief for the United States in Support of its Motion for Summary Judgment at 7 n. 4 (filed Jan. 23, 1984). Defendant has not, however, explained why paragraph 11 of the Kozak Affidavit was presented at all, given its position as to the admissibility of post-hoc statements by negotiators.

(Pet. App. 35a, n. 16). Having definitively committed itself to one position before the Claims Court on the admissibility of post-execution accounts of the Treaty negotiating process, the United States should not be permitted, on appeal, to again change its ground and adopt an entirely new position. Having conceded that the Kozak statement should not be considered in construing Article XV(2), the similar statements of Mr. Kozak's counterparts in Panama should also not be considered.[17]

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[17] The Claims Court was particularly disturbed by the fact that the Kozak affidavit had been submitted to Courts throughout the nation:

> Moreover, the Kozak Affidavit, in the very form presented to this

B. The Federal Circuit's Consideration Of Diplomatic Correspondence As New Evidence On Appeal Was Improper

Apart from the doctrine of judicial estoppel, the appellate level submission of the diplomatic correspondence was improper procedurally. Normally, material that is not part of the trial record cannot be considered on appeal. *Boone* v. *Chiles*, 35 U.S. 117 (1836). *Zell* v. *Jacoby-Bender, Inc.*, 542 F.2d 34 (7th Cir. 1976). The reasons for the prohibition are self-evident. Litigants are entitled to develop a trial record that includes all matters of fact and law that might be presented on appeal; trial courts should be given the first opportunity to rule on all contested matters of fact and law; and appellate Courts are ill-equipped to consider questions on which no record exists.

The Eleventh Circuit in *Harris*—based on the usual prohibition against introducing new evidence on appeal—refused to consider the same diplomatic correspondence tendered to and received by the Federal Circuit. The *Harris* court rejected the correspondence not because the court lacked power to judicially notice it, but because the correspondence required "additional explanation" (Pet. App. 76a). As we show below, that ruling was proper as a

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court, has been presented to other courts that have considered this issue. See n. 9 supra. Some of those courts have expressly relied on it. See, e.g., *Stabler* v. *United States*, No. CA3-83-0166-R, slip op. at 3 (N.D.Tex. Nov. 30, 1983); *Pierpoint* v. *United States*, No. 83-0354-2, slip op. at 5-6 (D.S.C. Oct. 3, 1983). Other courts may have been swayed by the affidavit without specifically mentioning it.

(Pet. App. 35a-36a, n. 16). As the Claims Court also noted (*id.*), this conduct resulted in substantial costs to the American public and the judicial system in litigating the Article XV(2) question:

> At least 42 lawsuits, involving perhaps hundreds of plaintiffs, have presented the issue to this and other courts. See n. 9 supra. The cost borne by the plaintiffs, the defendant and the judicial system in resolving this issue through piecemeal litigation has been, and will continue to be, substantial.

matter of law. The Federal Circuit's contrary ruling was error.

1. In a dispute over treaty interpretation, many aspects of the treaty's genesis and subsequent development may be considered. Section 147 of the Restatement of Foreign Relations Law (1965) lists nine permissible criteria for treaty interpretation including: the plain meaning of the agreement, the historical context of the agreement, the drafts and other documents submitted for consideration, the record of negotiations, the language of the treaty in any translation, and a comparison of the translations. Significantly, the Restatement does not include post-treaty diplomatic correspondence as an acceptable criteria.[18]

2. But assuming *arguendo* that post-treaty diplomatic correspondence is relevant, the Federal Circuit's judicial notice and consideration of the correspondence as conclusive of the Treaty interpretation issue was reversible error. To the extent it may be considered at all, the correspondence should not have been considered without affording the petitioners their rights to test and contest it on an adversary record. Such an opportunity is required, for example, by Rule 201(e) of the Federal Rules of Evidence, which provides that the opponent of evidence proposed to be noticed judicially must be heard on both the content of the evidence and the manner of its introduction.[19]

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[18] Article 31 of the Vienna Convention on the Law of Treaties (63 AJIL 875 (1969)) would appear to accept such post treaty correspondence as secondary criteria. The U.S. is not a party to the Vienna Convention.

[19] To the same effect is Rule 44.1 of the Claims Court rules (identical to the similarly numbered Federal Rule of Civil Procedure), which requires a party intending to raise an issue of foreign law to provide opponents with reasonable written notice of the issue. Rule 44.1 of the Federal Rules of Civil Procedure has been held to require prior notice of evidence relating to a foreign nation's interpretation of a bilateral treaty. See *United States* v. *VETCO*, 691 F.2d 1281 (9th Cir. 1981).

Before the Federal Circuit, the United States successfully urged that the correspondence be considered notwithstanding "the *arbitrary* rules that might normally govern discovery in a trial court or preclude an appellate court from reviewing information not considered by the lower court" (emphasis added). Opposition of the United States to Appellee's Motions to Strike, at 3, March 5, 1985. The Justice Department may characterize American civil procedure as it wishes, but the fact remains that those "arbitrary" rules embody the basic tenets of due process and fundamental fairness.

3. If those "arbitrary" rules had been applied, the Federal Circuit would have been required to consider the following points which were made in Petitioners' Motions to Strike (filed on March 4, 1985, prior to oral argument) and Petitioners' Petitions for Rehearing (filed on May 24, 1985, following the Federal Circuit's decision):

- In the transcript of a July 1984 meeting of the Commission's supervisory board, Dr. Fernando Cardoze—the author of the disputed diplomatic transmittal note—expressed the view that the U.S. citizen employees of the Commission should not receive any added compensation (by way of a cost-of-living-allowance) because they already were entitled to the substantial benefit of exemption from U.S. income tax;

- Two of the three letters that accompanied the Cardoze transmittal were written by individuals who were not present at the negotiating sessions that involved the

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As discussed above, the United States expressly declined the Claims Court invitation to procure such evidence. See also *Jannenga* v. *Nationwide Life Insurance Co.*, 288 F.2d 169 (D.C.Cir. 1961) (per Burger, J.) (party that sought the application of District of Columbia case law at trial prevented from arguing on appeal that trial court should have judicially noticed the law of Ohio or Missouri).

taxation of U.S. employees. Moreover, there is no evidence that any of the three was present at the session when Article XV(2) was accepted by Panama;

- Although Foreign Minister Cardoze says he consulted Dr. Aristides Royo (a negotiator for the Government of Panama, who was present at all the negotiating sessions), no letter from Dr. Royo was sent to the American Embassy with the other three;

- No inquiry was made of Dr. Carlos A. Lopez-Guevara, Panama's Ambassador Extraordinary and Plenipotentiary to the Treaty negotiations, whose affidavit had been of record in this litigation since March 8, 1984.

4. Nor was the Federal Circuit correct in equating the late introduction of the diplomatic correspondence below with the introduction, in *Sumitomo Shoji America, Inc.* v. *Avagliano*, 457 U.S. 176, 184, n. 9 (1982), of a diplomatic note from the Ministry of Foreign Affairs of Japan. The *Sumitomo* note was submitted on February 26, 1982, two months in advance of oral argument. (The Federal Circuit incorrectly characterized the filing of the *Sumitomo* note as occurring "within a few days of argument before the Court".)

As the *amicus curiae* brief of the United States in *Sumitomo* observed, the February 26, 1982 diplomatic cable from the Ministry of Foreign Affairs of Japan (MFA) was not submitted to establish a new interpretation of the disputed Treaty. That cable was simply a reaffirmation of the Ministry's previous view. See Appendix B to Brief for the United States as *amicus curiae* in the *Sumitomo* case.

The cable was submitted for the limited purpose of resolving an intra-mural squabble that surfaced during *Sumitomo* between the MFA and the Japanese Ministry of International Trade and Industry (MITI). The cable clarified that MFA and not MITI was the instrumentality within

the Government of Japan whose view should be deemed the official view:

> *Sumitomo* refers (Br. 20) to the brief *amicus curiae* filed by the Ministry of International Trade and Industry (MITI) of the Government of Japan in this case. The MITI brief does not specifically address the legal question of whether *Sumitomo* is a company of Japan for purposes of the Treaty. But because MITI's brief might be understood to support *Sumitomo*'s position on this issue, and in order to assist the Court by resolving any resulting confusion regarding the position of the Government of Japan on this issue we requested the State Department to seek clarification from MFA. The February 26, 1982 statement of MFA, reiterating its previous view (App. B, infra) is the result of that inquiry.

Brief for the United States as Amicus Curiae, *supra*, as reported on LEXIS at 14. *Sumitomo* cannot be read, as it was by the Federal Circuit, for the much broader proposition that a foreign government may, by diplomatic correspondence tendered to a U.S. court at any stage of its proceedings, create a retroactive interpretation of an extant treaty. As this Court ruled in *Sumitomo*, it is not proper to read a government's current view of a treaty as evidence of its original intent in entering into the treaty. *Sumitomo*, *supra*, at n. 10.

Moreover, the form of the diplomatic correspondence submitted below, i.e., 3 post-treaty statements by Panamanian negotiators, accompanied by a transmittal letter from Panama's then Foreign Minister, is dubious authority. As the Claims Court observed below (Pet. App. 36a, n. 16), it is far from clear whether a negotiator's post-treaty accounts of negotiating sessions are admissible to create, as the Federal Circuit did here, a retroactive interpretation. The O'Connors submit that such accounts should be subject to the bar against noncontemporaneous testimony

by legislators about legislative intent in enacting statutes. *City of Los Angeles* v. *Superior Court,County of Los Angeles*, 170 Cal. App. 3d 744, 216, Cal. Rptr. 311 (1985).

Nor should the Court overlook the fact that the United States was *amicus curiae* in *Sumitomo* and therefore a disinterested intermediary. Here, the United States' conduct must be viewed with a jaundiced eye, as it is not only a litigant, but it has a substantial financial interest in the outcome. Its conduct, therefore, must be subject to the customary restraints against the untimely introduction of "new evidence". See, for example, *Labadie Coal Co.* v. *Black*, 672 F.2d 92 (D.C. Cir. 1982). Such evidence should be subject to the healthy skepticism attaching to material tendered at the last moment and having no prior independent existence.

II. Article XV(2) Exempts U.S. Citizen Employees Of The Panama Canal Commission From U.S. Income Taxation On Their Commission Salaries

A. The Meaning Of Article XV(2) Is Clear And Should Be Given Effect

Treaties are contracts between nations. Like other contracts they are interpreted according to the rule that the plain meaning of a legal instrument is controlling, absent extraordinary reasons. *Sumitomo Shoji America, Inc.* v. *Avagliano*, 453 U.S. 176, 181 (1982); *Maximov* v. *United States*, 373 U.S. 49, 54 (1963); *Choctaw Nation of Indians* v. *United States*, 318 U.S. 423, 432 (1943); *Valentine* v. *United States*, 299 U.S. 5, 11 (1936); *Santovincenzo* v. *Egan*, 284 U.S. 30, 40 (1931); *United States* v. *Texas*, 162 U.S. 1, 36 (1896).

It is difficult to conceive of language with clearer meaning than Article XV(2). The category of persons to which it applies is expressly stated, and the nature of the exemption to which they are entitled is precisely delineated. Nowhere in the Treaty package is there treatment of the

same subject matter, nor is there other language that creates an ambiguity, or the latent possibility of one. The decision of the Claims Court was correct on these grounds alone. "Any taxes" means *any* taxes. The Claims Court below and the Eleventh Circuit in *Harris* were correct in so holding.

B. The Omission From Article XV(2) Of Limiting Language That Was Used Elsewhere In The Treaty And Agreement Requires That The Plain Meaning Be Given Effect

As noted by the Claims Court, the common-sense interpretation of the phrase "any taxes" in accordance with its plain meaning finds authoritative support in other provisions of the Treaty package. For example, the first paragraph of Article XV, which applies to the Commission, its contractors and subcontractors (but not the Commission's employees), provides that they "are exempt from payment *in the Republic of Panama* of all taxes . . . on their activities or property" (emphasis added).

In the case of paragraph three of Article XV, which deals with personal property, gift and inheritance taxes of U.S. citizen employees, the exemption also is limited by specific language. It provides that the mere presence of personal property of American employees "within the territory of the Republic of Panama . . . due solely" to their work for the Commission will not give rise to the host country's usual exercise of *in situ* tax jurisdiction.

The Treaty itself, in Article IX(9), provides another illustration of how the parties used specific terms to limit the application of the rule or restriction upon which they had agreed. Paragraph 9 pertains to vessels, cargo, passengers and crew that transit the Canal. It says that they "shall be exempt from any taxes, fees, or other charges *by the Republic of Panama*" (emphasis added). The provision goes on to say—demonstrating the particularity with which the negotiators treated taxation—that:

> The Republic of Panama may also require the passengers and crew disembarking from such vessels to pay such taxes, fees and charges as are established *under Panamanian law* for persons entering its territory (emphasis added).

Similarly, in paragraph 2(e) of Article XI of the Implementation Agreement, the income of the Commission's U.S. contractors (as distinguished from their activities and property, which are covered by Article XV(1)) is expressly made subject to Panama taxation unless it is taxed by the United States at a substantially equivalent rate. This section strongly suggests that the U.S. treaty negotiators were capable of being equally as precise if they had intended to retain for the United States the right to tax Americans on their Commission salaries.[20]

The Government has argued below that the repeated use of these explicit limitations in other parts of the Treaty agreements should permit the court to engraft similar language onto Article XV(2). The Claims Court correctly concluded, however, that such a radical departure from the plain meaning of Article XV(2) was unwarranted under applicable rules of treaty construction (Pet. App. 26a).[21]

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[20] The trial court discussed other provisions in the treaty documents where specific language was employed to create unilateral limitations (Pet. App. 23a-27a).

[21] When the Treaty was transmitted to the Senate by the Executive Branch (S. Exec. Rep. 95-12, 95th Cong., 2d Sess. 155 (1978)), it was accompanied by a section-by section analysis which stated that the provision here in dispute was intended to provide an exemption only from Panamanian taxes. In the courts below, the Government relied on that section-by-section analysis implying that it constituted contemporaneous legislative history as to the meaning of the provision. In fact, like the Kozak affidavit, the analysis was prepared after the Treaty. In addition, the Government conceded before the Claims Court that the analysis was prepared by State Department officers, Kozak and Geraldeen Chester, "who were not present at any of the negotiating

C. The Use By The United States Of Specific Limitations In Other International Agreements Demonstrates That This Was A Deliberate Omission

The Government suggested below the possibility of a drafting error. The Government argued that, although the U.S. negotiators were skilled, "even skilled persons do not always use the most precise language" (U.S. Government Brief to the Federal Circuit, filed November 30, 1984, p. 42). If it is the Government's explanation that this litigation stems from a drafting error, taxpayers submit that such a proposition is untenable. The record shows that ranking officials in the State and Treasury Departments participated in the preparation and negotiation of the U.S position. The Court may take notice that Ambassadors Ellsworth Bunker and Sol Linowitz, who conducted and concluded the negotiations with Panama, were experienced officers in the diplomatic service.

The truth of the matter is that the language of Article XV(2) is both special and unique. The Kozak affidavit (App. 87-90) says that it had its genesis in the standard Status of Forces Agreements (SOFA) reached by the United States with other countries. If that is so, then the substantive changes in wording from prior usage—which undeniably have changed the meaning—cannot reasonably be said to have been unintentional or inadvertent. This is seen by examining the corresponding provisions in various SOFA Agreements, while noting that the O'Connors know of no SOFA Agreement that is similar to Article XV(2). In the SOFA negotiated among the parties to the North

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sessions during which we know that the substance of Article XV was discussed" (Pet. App. 57a). Finally, the Claims Court properly observed that the issue was presented to the Senate by the Executive Branch without disclosure of any of the negotiating history showing that there was a serious binational question involved (Pet. App. 59a). Before the Senate, therefore, the issue appeared as one merely of domestic tax law which, as then Legal Advisor Hansell said, would be handled as "an internal matter" (U.S. App. 12a).

Atlantic Treaty (signed June 19, 1951 and entered into force August 23, 1953), the pertinent language of Article XI(1) states:

> Members of a force or civilian component shall be exempt from taxation *in the receiving State* on the salary and emoluments paid to them as such members *by the sending State* or on any tangible movable property the presence of which *in the receiving State* is due solely to their temporary presence there (emphasis added).

The supplementary agreement to the NATO Status of Forces Agreement pertaining to forces stationed in the Federal Republic of Germany was signed by seven countries on August 3, 1959 and entered into force July 1, 1963. In Part II of the agreement pertaining to Article 68, the following "agreed declaration" concerning German taxes appears at paragraph 2(a):

> Tax is imposed only on internal income, i.e., in general, income earned *within the Federal Republic*, except emoluments and income paid to members of a force or of a civilian component *by the sending State* in their capacity as such members (emphasis added).

A similar provision limiting the tax exemption of U.S. armed force members and the civilian component is contained in the 1960 Agreement Under Article VI of the Treaty of Mutual Cooperation and Security between Japan and the United States. Article XIII(2) of that Agreement provides:

> Members of the United States armed forces, the civilian component, and their dependents shall not be liable to pay *any Japanese taxes to the Government of Japan* or to any other taxing agency in Japan on income received as a result of their services with or

> employment by the United States armed forces (emphasis added).

The SOFA between Australia and the United States, in like manner, provides in Article 6(1), that:

> Income derived by a member of the United States Forces or of the civilian component from rendering services as a member to the United States Government in Australia, *shall be deemed not to have been derived in Australia*, provided it is not exempt, and is brought to tax, under the taxation laws of the United States (emphasis added).

Agreement Concerning the Status of United States Forces in Australia, signed May 9, 1963 and entered into force May 9, 1963. Article XIV(2) under Article IX of the Mutual Defense Treaty between the United States and the Republic of Korea (signed July 9, 1966 and entered into force February 9, 1967) similarly states:

> Members of the United States armed forces, the civilian components, and their dependents shall not be liable *to pay any Korean taxes to the Government of the Republic of Korea or to any other taxing agency in the Republic of Korea* on income received as a result of their service with or employment by the United States armed forces, including the organizations provided for in Article XIII (emphasis added).

Further illustrating the fact that Article XV(2) was a special departure from established U.S. Government policy is the Convention Between the United States and Egypt, signed August 24, 1980 (T.I.A.S. 10149). That agreement, executed three years *after* Article XV(2), continues the pattern of the pre-Panama Canal treaty tax provisions discussed above. Article 21(1) of that Agreement states:

> Wages, salaries, or similar remuneration, including pensions, annuities, or similar benefits paid from public funds of one of the Contracting States:

(a) To a citizen of that Contracting State, or
(b) To a citizen of a State other than a Contracting State who comes to the other Contracting State expressly for the purpose of being employed by the first-mentioned Contracting State

for labor or personal services performed as an employee of the national Government of that Contracting State, or any agency thereof, in the discharge of functions of a governmental nature *shall be exempt from tax by the other Contracting State* (emphasis added).

Given this depth of U.S. Government experience in drafting tax provisions in treaties, it may properly be concluded that the U.S. negotiating team simply could not have been so lacking in knowledge as to have adopted Article XV(2) without intending to create a binational exemption. As stated so aptly in *Santovincenzo* v. *Egan*, 284 U.S. at 37 "[t]he omission from Article VI of the Treaty with Persia of a clause of this sort, so frequently found in treaties of this class, must be regarded as deliberate".

D. The Federal Circuit Erred In Refusing To Consider Other Official Statements By Panama That Support The Construction Of Article XV(2) As A Binational Exemption

The admissibility of the diplomatic correspondence from Panama is treated in Point I of this brief. Even if *arguendo* the correspondence might be admissible from a procedural standpoint, it was improper for the Federal Circuit to consider that material alone. The papers consisted of almost identical letters from three former Panamanian negotiators. These letters were delivered, in February 1985, to the U.S. Embassy in Panama with a brief transmittal note from then Foreign Minister, Dr. Fernando Cardoze (U.S. App. 4a-9a). The thrust of the note and the letters is that the Ministry's position at that time coincided with that of the State Department.

On March 4, 1985, the O'Connors filed a motion to strike the correspondence. Attached to their motion was a transcript of certain remarks made in July 1984 by the then Foreign Minister of Panama (Mr. Oyden Ortega) and by Dr. Fernando Cardoze (the person later to succeed Mr. Ortega and who, as Foreign Minister, signed the note that transmitted the three letters). The transcript was from the official record of a meeting of the Commission's nine-member supervisory board (*supra*, pp.18, 30) established under Article III(3a) of the Canal Treaty and Pub.L. 96-70, §1102, Sept. 27, 1979, 93 Stat. 456, 22 U.S.C. §3612.

The question under discussion was whether U.S. citizen employees should be given a cost of living allowance (COLA) to compensate them for the impending loss of their postal, commissary and post exchange privileges to take place in October 1984 pursuant to Article XIII(3) of the Implementation Agreement. Under §1206 of Pub.L. 96-70, the Commission had permissive authority to grant such a COLA. The four Panamanian members of the board were adamantly opposed to extending such a benefit, principally because it would create a disparity in treatment between U.S. and Panamanian employees. Dr. Cardoze expressed the view that the exemption from U.S. income taxation created by the Treaty was the form of "special compensation" that the U.S. citizen employees should receive:

> I think the U.S. negotiators were wise, and just as the Panamanian negotiators extablished that the privileges would be eliminated—why did they do that? Because they knew that would be an irritant in the relationship. Likewise, the American negotiators were very wise. They looked for a manner in which they could give a compensation to the U.S. employees, in fact much more than the COLA could give. There is a clause that says the U.S. citizen will not pay taxes for the salaries that they earn from the Panama Canal Commission.

> So if you believe that it is necessary to grant an additional compensation, then let's not make a mistake. Let us give them—let's give this additional compensation to all employees, or if you want to give a special compensation to the U.S. citizens who were here prior to October 1, 1979, and who are going to lose their privileges, then let us look for it in the U.S. treasury, and probably in the Treaty is already a basis for such a benefit.

At the board's session on the following day, Minister Ortega commented as follows:

> MINISTER ORTEGA: (Through the interpretor) It happens, Mr. Chairman, that in my interventions previously, Dr. Cardoze had expressed the aspect related to the income tax matter that could be something that—could be an exemption for the U.S. citizen, and that undoubtedly this would be a form of—it would be a real economic compensation.

At these board meetings, Minister Ortega and Dr. Cardoze both were participating officially on behalf of their Government in the management of the Panama Canal as contemplated by Article III of the Treaty. They were also speaking on a matter directly related to the interpretation of Article XV(2).[22] Their statements, clearly within the rule set out in *United States* v. *Reynes*, 50 U.S. (9 How.) 127, 147-48 (1850), should have been accepted by the Federal Circuit as more persuasive evidence of Panama's position than any other submission in the case.

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[22] These meetings were under the Chairmanship of U.S. Assistant Secretary of the Army William R. Gianelli. Only some two months earlier (on May 4, 1984), Secretary Gianelli had written a three page official letter to Assistant Secretary of State Langhorne A. Motley urging that the Executive Branch agree that Article XV(2) did in fact create a binational tax exemption. Secretary Gianelli's letter was attached as Appendix 6 to the O'Connor brief in the court below.

Such a conclusion becomes even more compelling upon careful analysis of the three letters. In the case of Mr. Jaime Arias (U.S. App. 9a), he claimed to have had a role only in the negotiation of Article XVI(2) (which is in the SOFA that implements Article IV of the Treaty), implicitly admitting that he was not involved with Article XV(2). As for Drs. Ahumada and Escobar, they stated that Articles XV(2) and XVI(2) in question "were discussed, negotiated, and drafted exclusively with respect to the tax exemptions that . . . Panama would grant." Unlike Dr. Lopez-Guervara, however, neither individual states that he participated in the negotiations where these articles were adopted. Indeed, the record contains no evidence that Dr. Ahumada ever participated in any of the meetings on the question of taxation.

If the Court should conclude that the tendered diplomatic correspondence is admissible at all, the O'Connors urge that, in any event, it should be considered side-by-side with the diametrically inconsistent opinions expressed by Minister Ortega and Dr. Cardoze only seven months before.[23]

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[23] The interpretation of Article XV(2) as a binational tax exemption is further supported by the statute that was passed to implement the Treaty package. Prior to the Treaty's entry into effect on Oct. 1, 1979, a *tax allowance* was paid U.S. citizen employees of the Canal agency pursuant to 2 C.Z.Code §146(1), 76A Stat. 17. The authority for payment of that allowance was repealed by the Treaty-implementing legislation, §3303(a)(1) of Pub.L. 96-70, 93 Stat. 499, 22 U.S.C. §3602, Sept. 27, 1979. The Commission, in turn, published regulations on Oct. 2, 1979, to deny the tax allowance to newly-hired U.S. citizens. 44 Fed.Reg. 56693. Subsequently, the Commission eliminated the allowance with respect to *all* U.S. citizen employees. 45 Fed.Reg. 59150, Sept. 8, 1980. See 35 CFR 134(b), Dec. 1979 ed.

Repeal of the tax allowance, which became superfluous in view of the tax exemption, constituted a *practical construction* of Article XV(2) by Congress consistent with the interpretation of Article XV(2) as a binational tax exemption. In an appropriate case, subsequent legislative action may demonstrate what intent underlies the initial enactment.

E. The Cases Relied On By The Government Are Inapposite

The appellate court below based its decision almost entirely upon the three letters that the State Department received from then Panama Foreign Minister Cardoze and transmitted to the Court of Appeals one working day before the oral argument. In doing so, the Court failed to acknowledge that the words "any taxes" as used in Article XV(2) can reasonably be interpreted in only one way. The Court concluded simply that its role was "limited to giving effect to the intent of the Treaty parties" (Pet. App. 6a) as disclosed in the three letters. By doing so, the Court ignored the applicability of the plain meaning rule and, with nothing more than a single sentence of its opinion, dismissed the extended, careful discussion by the Claims Court of the plain meaning rule as it affects this treaty dispute.

In a concurring opinion, three of the five-member panel below expressed the view that the letters were not essential to their decision in favor of the Government. Their conclusion also ignored the text and plain meaning of Article XV(2). Rather than construing the language, they judicially engrafted on the title of the article (i.e., "Taxation") the words "by the Republic of Panama" (Pet. App. 8a).

In the proceedings below, the Government repeatedly asserted that the plain meaning of the Implementation Agreement need not be followed if the result would be contrary to the intent of the signatories. In support of that contention, the Government cited this Court's decisions in the following cases: *Sumitomo Shoji America, Inc.*

"We regard the action of the Congress, following that of the State, as a practical construction of the treaty. . . ." *Pigeon River Improvement, Slide & Boom Co.* v. *Charles W.Cox, Ltd.*, 291 U.S. 138, 160-61 (1934).

v. *Avagliano*, 457 U.S. 176 (1982); *Maximov* v. *United States*, 373 U.S. 49 (1963); *United States* v. *Texas*, 162 U.S. 1 (1896); and *Ross* v. *McIntyre*, 140 U.S. 453 (1891).

Examination of these decisions reveals that in none of them does the actual holding stand for the proposition espoused by the Government. The Government relies principally on *Sumitomo* and places special emphasis (as did the Federal Circuit) on the portion of the opinion which reads: "Our role is limited to giving effect to the intent of the Treaty parties." 457 U.S. at 186. Both the Government and the Federal Circuit, however, overlook the subsequent statement that delineates what the Court actually held:

> When the parties to a treaty both agree as to the meaning of a treaty provision, *and that interpretation follows from the clear treaty language*, we must, absent extraordinarily strong contrary evidence, defer to that interpretation (emphasis added).

In *Sumitomo*, which involved only private litigants, the Government appeared as *amicus curiae*, as noted above (*supra* at 31-33), and presented a cable from Japan which reaffirmed that country's earlier opinion. The opinion agreed upon by the U.S. and Japan accorded with the plain meaning of the clause in question, and the Court held that it should be so construed. There is a crucial difference between that situation and the case at bar. Here the Government asserts that Article XV(2) *does not mean what it says* and that Panama now shares the same view. The result and reasoning of *Sumitomo* do not support the Government's theory that the plain and obvious meaning of the words "any taxes" may be altered merely because the two governments are said to have arrived at that conclusion in February 1985, seven years after the article was agreed upon.

Examination of the three other decisions also reveals that none of them supports the Government's position. In

Maximov, this Court considered a tax treaty which exempted residents of the United Kingdom from U.S. capital gains taxation. It held that the plain meaning of the term "resident of the U.K." should be given effect and a tax exemption was denied to the claimant trust that was a resident of the U.S., although with U.K. beneficiaries. The opinion by way of dicta said:

> . . . it is particularly inappropriate for a court to sanction a deviation from the clear import of a solemn treaty between this Nation and a foreign sovereign, when, as here, there is no indication that application of the words of the treaty according to their obvious meaning effects a result inconsistent with the intent or expectations of its signatories. 373 U.S. at 54.

In *United States* v. *Texas*, as noted above, the Court stated that the intention of the two governments, gathered from the words of the treaty, must control. The decision shows, however, that there were complex questions raised by the nonconformity of the treaty text with a map to which it made reference. Those ambiguities meant that there was *no plain meaning* that could be given effect—making it necessary for the Court to construe the disputed language by referring to objective geographic data.

Ross v. *McIntyre* required the interpretation of two treaties between the U.S. and Japan, entered into in 1857 and 1858, to determine whether the American Consul General had jurisdiction to try a U.S. citizen for a crime committed in Japan. It was necessary to resolve an ambiguity raised by the second treaty. Application of plain meaning, such as is presented in the present case, was not at issue.

None of the cases relied upon by the Government below supports the alteration of language sense where, as here, there is no ambiguity and the subject matter does not appear elsewhere in the treaty documents. This is an instance, it is submitted, where no applicable precedent or principle permits the treaty terms to be narrowed. "As

treaties are contracts between independent nations, their words are to be taken in their ordinary meaning 'as understood in the public law of nations.' " *Santovincenzo* v. *Egan*, 284 U.S. at 40. The O'Connors urge the Court to apply here the elementary canon of construction that it used in interpreting a provision of the Civil Rights Act of 1964, when it said:

> [T]he plain, obvious and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover.

Chandler v. *Roudebush*, 425 U.S. 840, 849 (1976).

F. The History And Tenor Of The Treaty Negotiations Confirm That Article XV(2) Is A Binational Tax Exemption

As indicated above, Panama was adamantly opposed to the notion that it should be barred from taxing United States citizens who lived and worked in Panama as PCC employees. As late as July 14, 1977, Panama insisted that such employees, who would enjoy all the governmental services of the new sovereign, must pay their fair share of taxes to Panama.

In all previous Article XV(2) litigation, the United States maintained that, notwithstanding the exemption from "any taxes" contained in Article XV(2), the negotiations ended in mid-August 1977 with Panama acceding to the U.S. demand that the PCC income of U.S. citizen employees be off-limits to Panamanian taxation. As shown below, however, such a result is inconsistent with the course and tenor of the Treaty negotiations, and the long, stormy history of Panama-U.S. relations. The negotiating history clearly suggests that Article XV(2)'s object was to establish a binational tax exemption as a compromise between the sharply divergent Panamanian and American positions.

1. The precise language of Article XV(2) was adopted from a parallel provision of Article XVI(2) of the Implementation Agreement of Article IV of the Treaty, governing the status of U.S. Forces in Panama. The language of the Article IV Implementation Agreement is almost identical to the language of Article XV(2) except that, in the second sentence, an explicit reference is made to taxation "as is provided by Panamanian law":

> Members of the Forces or the civilian component, and dependents, shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the United States Forces or for any of the service facilities referred to in Articles XI or XVIII of this Agreement. Similarly, *as is provided by Panamanian law* they shall be exempt from payment of taxes, fees, or other charges on income derived from sources outside of the Republic of Panama (emphasis added).

An earlier draft of the Article XV(2) language, dated June 26, 1977, contained the identical second sentence reference to taxation "as is provided by Panamanian law".

The final text (supra, pp.3,36) shows that the language ultimately agreed to by Panama and the United States in Article XV(2) was purged of all reference to "Panamanian law".

Given the absence of a negotiating record for the sessions at which Article XV(2) was adopted, it may never be definitively ascertained why the terminology "as provided by Panamanian law" was dropped from Article XV(2) but retained in the parallel Implementation Agreement for Article IV of the Treaty. The circumstances suggest, however, that the elimination from Article XV(2) of the only language referring to *either* Treaty party was intended to leave absolutely no question but that the Article XV(2) exemption was applicable to *both* Treaty parties.

2. Interpretation of Article XV(2) as a compromise formulation, exempting the U.S. citizen PCC employees from taxation by *both* Treaty parties, is fully consistent with the political agenda of each of the negotiating parties. From the Panamanian point of view, mutual acceptance of a binational tax exemption would confer special recognition on the binational status of the Panama Canal Commission, which Panama viewed as a partnership of equals. It would also erase any lingering doubt that the U.S. intended to assert, by the taxation power, continuing "colonial" authority over the Canal area.

From the perspective of the United States, a binational exemption would avoid the undesirable precedent of Panamanian taxation of the income of Americans employed by the Panama Canal Commission. It also would avoid the danger (noted by Ambassadors Bunker and Linowitz) that giving Panama the right to tax these U.S. employees might be used by treaty opponents to oppose ratification.

3. For both nations, a binational tax exemption was a relatively inexpensive solution to the impasse. Panama, of course, had never taxed income earned by U.S. citzen employees of the former "Canal Zone". Accordingly, Panama lost nothing by negotiating away the power to tax them. And, as discussed above, such salaries, historically, have been either free of U.S. tax prior to 1951 or taxed at a lower effective rate thereafter. Moreover, the fiscal impact on the U.S. was even further diminished because the pool of U.S. citizen-employees potentially benefiting from the exemption would, by operation of the Treaty, progressively diminish and, by the year 2000, disappear. Also, the U.S. negotiators, in general, viewed the taxation dispute as a political problem largely bereft of any real economic significance.[24]

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[24] In contrast to these tenable explanations for the compromise, the Government in its Reply Brief in *Harris* (at p. 7, n.4), was unable to offer any explanation of why Panama allegedly capitulated, stating that:

4. Finally, a tax exemption for U.S. citizen PCC employees was a modest cost compared with the other economic concessions made by the United States to Panama in the Treaty package. In all, the United States obligated itself: to pay Panama an annuity which would increase from $50 or 60 million annually to $80 or 90 million annually when the treaty terminates in 1999; to secure approximately $300 million in aid credits for Panama; and to turn over to Panama property previously owned by the U.S. Government having an estimated replacement value of $8 billion. *See* S. Exec. Rep. 95-12, 95th Cong., 2d Sess. (1978) at 91 *et seq.* The modest tax exemption conferred by Article XV(2) is entirely consistent with the pattern of other economic concessions provided for in the Treaty package.

CONCLUSION

For the foregoing reasons, the decision of the United States Court of Appeals for the Federal Circuit should be reversed.

ALLAN I. MENDELSOHN
MARVIN L. SZYMKOWICZ
WARD & MENDELSOHN, P.C.
1100 17th Street, N.W.
Suite 900
Washington, D.C. 20036
(202) 785-0200
Counsel for Petitioners

Of Counsel
DWIGHT A. MCKABNEY
Apartado 3116
Balboa-Ancon
Republic of Panama
011-507-63-5316

"Exactly why the Panamanians accepted the U.S. position may never be known with certainty".